

Message Text

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ACTION EB-04

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FM AMEMBASSY PARIS
TO DEPARTMENT OF TREASURY
SECSTATE WASHDC 8223

C O N F I D E N T I A L SECTION 01 OF 02 PARIS 08018

LIMDIS GREENBACK

E. O. 11652: GDS
TAGS: EFIN, FR
SUBJECT: PARIS FOREX MARKET AND THE ELECTIONS

1. WITH JUST FIVE DAYS TO GO BEFORE THE FIRST ROUND OF THE ELECTIONS, THERE STILL IS NO SIGN OF PRESSURE ON THE FRANC INDUCED BY SHIFTS OF CAPITAL OR BY CHANGES IN FRANC POSITIONS. THE FRANC EXCHANGE RATE CONTINUES TO TRACK THE DOLLAR, STRENGTHENING AGAINST THE DOLLAR WHEN THE DOLLAR WEAKENS AGAINST THE D/MARK AND VICE-VERSA WHEN THE DOLLAR STRENGTHENS AGAINST THE D/MARK AS OCCURRED YESTERDAY, MARCH 6. THIS MEANS THAT WHEN THE FRANC WEAKENS AGAINST THE DOLLAR IT STRENGTHENS AGAINST D/MARK AND VICE-VERSA WHEN IT IS STRONGER AGAINST THE DOLLAR. THUS, TAKING THE FRANC/DOLLAR AND THE FRANC/D-MARK RATES INTO ACCOUNT, THERE IS NO PARTICULAR SIGN EVEN IN EXCHANGE RATE TERMS OF A WEAKER FRANC DURING THE PAST SEVERAL WEEKS. BOF INTERVENTION HAS BEEN MINIMAL IN RECENT DAYS.

2. MOF SOURCES HAVE CONFIRMED TO FINATT THAT EMERGENCY CONTROL MEASURES ARE READY AND COULD BE IMPLEMENTED
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"WITHIN HOURS" AFTER INSTRUCTIONS TO DO SO, JUST IN CASE SOMETHING HAPPENS. THESE MEASURES, AS REPORTED EARLIER, INCLUDE A WIDE RANGE OF POSSIBLE CONTROLS, MAINLY FEATURING: A TWO TIER FOREX MARKET, SUSPENSION OF THE FORWARD MARKET, CONTROLS ON ACQUISITION OF FOREIGN SECURITIES BY FRENCH RESIDENTS, STRICT REGULATION OF BANK FOREX POSITIONS, CREDIT CONTROLS

ON DOMESTIC FRANC BORROWING TO MAKE ADVANCE IMPORT PAYMENTS, SUSPENSION OF BOF MONEY MARKET REDISCOUNT FACILITIES, A PENALTY RATE FOR BOF PURCHASE OF FRANC CURRENCY REMITTED FROM ABROAD, ETC. MOF SOURCES INDICATE THAT A SERIOUS EFFORT WOULD BE MADE TO DEFEND THE FRANC DURING THE ELECTORAL PERIOD BUT THAT SUCH DEFENSES DO NOT ENVISION A PARTICULAR EXCHANGE RATE OR MASSIVE INTERVENTION AT SOME SUPPORT POINT. IF NECESSARY, THE FRANC EXCHANGE RATE WILL MOVE. THE MOF'S CLEAR INTENTION IS TO MAKE ANY POSITIONS TAKEN AGAINST THE FRANC AS EXPENSIVE AND AS RISKY AS POSSIBLE AND THEIR MAJOR OBJECTIVE IS TO PREVENT THE DEVELOPMENT OF LEADS AND LAGS, WHICH EXPLAINS THE EMPHASIS UPON FRENCH FRANC CREDIT AND SUSPENSION OF MONEY MARKET REDISCOUNT FACILITIES IN THE PACKAGE OF CONTROLS.

3. FROM AN ANALYTICAL VIEWPOINT, NET CAPITAL FLIGHT MUST BE BASED ON SUBSTANTIAL SOURCES OF FUNDS. THERE ARE BASICALLY THREE POSSIBILITIES: EXTERNAL POSITIONS HELD BY NON-RESIDENTS IN FRENCH FRANCS; THE FLOW OF TRADE, SERVICE, AND CAPITAL RECEIPTS AND PAYMENTS (ABOUT 8 BILLION DOLLARS EACH WAY EACH MONTH IN FRANCE); AND TOTAL FINANCIAL ASSETS HELD BY FRENCH RESIDENTS. WHILE CHANGES IN EXTERNAL POSITIONS IN FRENCH FRANCS COULD AFFECT THE EXCHANGE RATE, THIS IS A RELATIVELY CONFIDENTIAL

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SMALL SOURCE OF FUNDS FOR SPECULATIVE PURPOSES AND DOES NOT SEEM TO CONCERN MOF OFFICIALS. THE POTENTIAL LEADS AND LAGS BASED ON THE ONGOING FLOW OF PAYMENTS AND RECEIPTS FOR TRADE, SERVICES, AND CAPITAL CLEARLY IS THE MAJOR CONCERN AND IS REFLECTED IN THE PACKAGE OF CONTROL MEASURES READY ON A STANDBY BASIS. THE POSSIBILITY OF MASSIVE CHANGES IN FINANCIAL ASSETS HELD BY FRENCH RESIDENTS IS DISCOUNTED BY MOF OFFICIALS. ACCORDING TO ONE MOF SOURCE, "THIS IS NOT L968 WHEN

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C O N F I D E N T I A L SECTION 02 OF 02 PARIS 08018

LIMIDS GREENBACK

EVERYONE WAS SURPRISED ONE FINE MORNING BY THE POSSIBILITY OF A REVOLUTION AND REACTED IN A KIND OF PANIC. THIS IS AN ELECTION. EVERYONE HAS KNOWN ABOUT IT FOR MONTHS, INCLUDING THE POSSIBILITY OF A VICTORY BY THE LEFT. WE DON'T SENSE A PANIC REACTION. IN FACT, THERE HAS BEEN LESS OF THIS KIND OF ACTIVITY SO FAR THAN WE EXPECTED. IN THIS RESPECT, THINGS ARE REALLY QUITE CALM."

4. MOST FOREX MARKET TRADERS EXPECT SOME MOVEMENT AGAINST THE FRANC DURING THE ELECTION PERIOD, PARTICULARLY DURING THE WEEK BETWEEN THE FIRST AND SECOND ROUNDS. MOF OFFICIALS WOULD NOT DISAGREE WITH THIS VIEW BUT SEEM CONFIDENT OF THEIR ABILITY TO COPE WITH THE KIND OF PRESSURE THEY CONSIDER MOST LIKELY. THERE IS VERY LITTLE SIGN OR INDICATION FROM ANY SOURCE OF A MASSIVE CHANGE IN FINANCIAL ASSETS HELD BY FRENCH RESIDENTS. IF THIS ELEMENT REMAINS THE SAME DURING THE ELECTORAL PERIOD, MOF CONTINGENCY PLANS AND EXPECTATIONS WOULD BE SOUNDLY BASED; AND THERE IS NO REASON TO DOUBT THEIR ABILITY TO MAKE SPECULATION BOTH VERY EXPENSIVE AND RISKY, PARTICULARLY FOR FRENCH RESIDENTS; AND FOR THIS REASON THE FRANC COULD WEATHER THE ELECTORAL PERIOD IN
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REASONABLY GOOD SHAPE. WHAT HAPPENS NEXT FOR THE FRANC DEPENDS UPON WHO WINS THE ELECTION, IN WHAT CIRCUMSTANCES AND UPON THE COMPOSITION AND POLICIES OF THE NEXT GOVERNMENT.

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